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IN THE

# Supreme Court of the United States

OCTOBER TERM 1941

No. 144.

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WM. CARNEGIE EWEN, LEWIS L. CLARKE, M. D. ADAMS and GEORGE E. WILE, as members of a duly constituted Income Bondholders' Protective Committee, and CHARLES S. ARONSTAM, Counsel to the Committee,

*Petitioners,*

against

THE PEORIA AND EASTERN RAILWAY COMPANY,

*Respondent.*

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## PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES DISTRICT COURT FOR THE SOUTHERN DISTRICT OF NEW YORK

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CHARLES S. ARONSTAM,
*Counsel to Petitioners.*

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## PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES DISTRICT COURT FOR THE SOUTHERN DISTRICT OF NEW YORK

*To the Honorable the Chief Justice and the Associate Justices of the Supreme Court of the United States:*

Your petitioners respectfully show to the Court as follows:

Petitioners Wm. Carnegie Ewen, Lewis L. Clarke, M. D. Adams and George E. Wile were duly appointed by the holders of Income Bonds of The Peoria and Eastern Railway Company as a Protective Committee to represent their interests in these proceedings (hereinafter referred to as the "Committee"). Petitioner Charles S. Aronstam was duly appointed as counsel to the Committee.

This is a petition for a writ of certiorari to review that portion of the Order Supplemental to Decree of the District Court of the United States for the Southern District of New York, convened as a special court of three judges, which dismissed the petitions of the Committee and its counsel for allowances for their services and reimbursement for their expenses in connection therewith "on the ground that the Court is without jurisdiction to grant such allowances".

## Summary Statement of the Matter Involved

These proceedings were initiated upon the petition of The Peoria and Eastern Railway Company (hereinafter referred to as the "Peoria Company") pursuant to Chapter XV of the Bankruptcy Act for the approval and confirmation of a Plan of Adjustment for (a) the Extension of the Date of Maturity from April 1, 1940, to April 1, 1960, of a Part of the Principal of the Peoria Company's First Consolidated Mortgage Bonds, dated February 22, 1890, and (b) for the Renewal and Modification of the Operating Agreement between the Peoria Company and the Cleveland, Cincinnati, Chicago and St. Louis Railway Company (hereinafter referred to as the "Big Four"), dated February 22, 1890, which expired on April 1, 1940.

The Special Court fixed the date for the hearing on said Plan of Adjustment for April 29, 1940, at which time the Committee applied for intervention in the proceedings. The application was granted and an order of intervention was duly made and entered on May 8, 1940.

The Committee, through its counsel, actively participated in all the hearings before the Special Court. Counsel has devoted almost a year of unremitting labor for the protection of the Income Bondholders and incurred disbursements in excess of One thousand dollars ($1,000).

On July 29, 1940, the Special Court made and entered a decree approving the Plan of Adjustment with certain

modifications insisted upon by the Committee, to wit: (1) the Income Bondholders shall have one director to represent their interests on the Board of Directors of the Company as long as the Income Bonds are outstanding, and (2) all questions concerning the amounts and validity of the accounts between the Big Four, the New York Central Railroad Company and the Peoria Company were specifically left open and reserved for further determination.*

On January 13, 1941, petitioners petitioned the Special Court for an order granting to them a reasonable allowance for their services and for the disbursements incurred by them in connection therewith. No answer to the petitions were filed by the Peoria Company, but upon the oral argument its counsel objected to the granting of allowances to petitioners on the ground that the Court had no jurisdiction to award same. The Special Court, in an opinion dated April 3, 1941, dismissed the petitioners' requests on the ground that the Court was without jurisdiction to grant any allowances to others than the Peoria Company under the provisions of Chapter XV of the Bankruptcy Act, citing as authority the opinion rendered *In re Baltimore and Ohio R. R. Co.*, 34 Fed. Supp. 154.

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*In the Order Supplemental to Decree, the Special Court modified its decree so as to provide, with respect to the inter-company accounts, as follows:

> "Section 24. All questions concerning the amount and validity of the accounts between the 'Big Four', the New York Central Railroad Company and the Petitioner are not determined in these proceedings and are hereby specifically left open and reserved for future determination. Should the New York Central Railroad Company and/or the 'Big Four' seek or attempt, in any year or at any time or times hereafter, to withdraw any part of the earnings or assets of the Petitioner by way of recoupment or repayment of said inter-company accounts, then and in such event said New York Central Railroad Company and/or 'Big Four', *upon objection by the representative of the Income Bondholders elected to the Board of Directors, must prove and establish their right to do so.*"

It is conceivable that the aforesaid section of the decree secured at the instance of the Committee may result in saving the Peoria Company a substantial portion, if not all, of the $2,500,000 alleged to be due and owing to the New York Central on account of advances.

## The Opinion of the Court Below

The opinion of the Special Court of the United States District Court for the Southern District of New York is reported in 37 Fed. Supp. 917. The portion of the opinion with respect to allowances is printed as Appendix A annexed hereto.

## Jurisdiction

The jurisdiction of this Court to grant the writ of certiorari applied for rests upon Section 745 of Chapter XV (11 U. S. C. A. 1245), which reads as follows:

> "Any final order or decree of the special court may be reviewed by the Supreme Court of the United States upon application for certiorari made by any person affected by the plan who deems himself aggrieved within sixty days after the entry of such order or decree, pursuant to the provisions of the Federal Judicial Code."

## Specification of Errors

The Special Court erred in determining that, under the provisions of Chapter XV of the Bankruptcy Act, it did not have jurisdiction to grant allowances to the Committee and its counsel for their services rendered herein and to reimburse them for their disbursements incurred in connection therewith.

The Special Court erred in determining that Section 725(6) of Chapter XV of the Bankruptcy Act (11 U. S. C. A. 1225[6]) is a limitation on the powers of the Special Court to award allowances and disbursements to those who have rendered necessary and beneficial services to the Court, the Peoria Company and its security holders.

## Question Presented

The only question presented is whether the Special Court had jurisdiction under Chapter XV of the Bankruptcy Act to grant allowances to the Committee and its counsel for their services and to reimburse them for their disbursements incurred in connection therewith.

The following excerpt from the opinion of the Special Court clearly indicates that the services rendered herein by the said Committee and its counsel were necessary and beneficial to the Peoria Company and its security holders:

> "We cannot, however, close our opinion without telling counsel for the two intervenors that we welcomed their participation in this cause, that by the modifications in the plan which they suggested, in our opinion, *they made a valuable contribution to the creation of a fair and reasonable adjustment herein under which the parties will have to operate for many years to come, and that if we had felt that we were authorized by Chapter 15 of the National Bankruptcy Act to grant them or their counsel a reasonable allowance, we should have done so.*" (Italics ours.)

The Special Court in its opinion on the merits of the Plan of Adjustment, reported in 34 Fed. Rep. 332, said, as follows:

> "The income bondholders occupy much the same position as preferred shareholders, *and as such they have a very lively interest in the payment of the accumulated advances.* We think that they should have representation upon the road's board of directors, so that they may continually keep advised of its affairs without the mediation of a court. * * * All they need is someone who will have the absolute right to scrutinize the road's operation, management and finances. *Hence we will modify the plan by virtue of the power given us* * * * " (at p. 338). (Italics ours.)

## Reasons for Granting the Writ of Certiorari

### I

**The Special Court had the power to grant the Committee and its counsel allowances for the necessary and beneficial services they rendered herein.**

Section 700 of Chapter XV of the Bankruptcy Act (11 U. S. C. A. 1200) provides as follows:

> "In addition to the jurisdiction otherwise exercised, courts of bankruptcy shall exercise original jurisdiction, as provided in this chapter, for postponements or modifications of debt, interest, rent, and maturities or for modifications of the securities or capital structures of railroads."

Section 713 of Chapter XV (11 U. S. C. A. 1213) provides as follows:

> "* * * Such three-judge court shall be vested with and shall exercise all the powers of a district court sitting in equity, and all the powers as a court of bankruptcy necessary to carry out the intent and provisions of this chapter, including the classification of claims at such time and in such manner as the court may direct."

The Special Court was therefore vested with all the powers of an equity and bankruptcy court, without limitation, insofar as the exercise thereof was necessary to the carrying out of the intent and provisions of Chapter XV.

Section 725(3) provides, among other things, that, before the Special Court may approve the adjustment, it must find:

> "(3) * * * that the plan is fair and equitable as an adjustment, *affords due recognition to the rights of each class of creditors* * * *" (Italics ours.)

In the instant case, in order for the Special Court to determine that the adjustment was fair and equitable and

afforded due recognition to the rights of the Income Bondholders, it was necessary that they be represented at the hearings by the Committee and its counsel; otherwise the Special Court could not have been able to determine their rights as a class of creditors. The Special Court recognized this necessity when it made an order permitting the Committee to intervene in these proceedings. The Court had before it the written consents of the First Mortgage Bondholders and the approval of the common stockholders to the adjustment, but there was nothing in the record that set forth the interest and rights of the Income Bondholders as the Peoria Company did not have to secure their written consents to the said adjustment. *The Special Court became aware of the rights of the Income Bondholders only through the intervention of the Committee and the presentation and argument of its counsel.* The modifications to the Plan of Adjustment were made by the Special Court solely by reason of the Committee's intervention herein. No other opportunity was afforded to the Income Bondholders in these proceedings to protect their interests as a class except by the representation of this Committee and its counsel.

Under the aforesaid circumstances it is inconceivable that the beneficial results secured to the Peoria Company and its creditors should be uncompensated by the Special Court sitting as a court of equity, when the Court itself said unequivocally that the Committee and its counsel made "valuable contribution to the creation of a fair and reasonable adjustment herein under which the parties will have to operate for many years to come". The Special Court, having permitted the petitioners to intervene herein and having utilized the services of the Committee and its counsel in modifying the Plan so as to be fair and equitable as an adjustment affording due recognition to the rights of all the creditors, had the power, under Section 713 (11 U. S. C. A. 1213), as a court of equity, to grant to them allowances for their meritorious services. These services as indicated by the Special Court itself were necessary to

enable it to carry out the intent and provisions of Chapter XV. The Peoria Company and its creditors having received the benefits derived from these services, sound equitable principles require that in good faith and conscience compensation should be allowed therefor.

Mr. Justice Sutherland, in discussing Section 77 of the Bankruptcy Act in *Continental Illinois National Bank & Trust Co.* v. *Chicago, Rock Island & Pacific Ry. Co.*, 294 U. S. 648, said, as follows:

> "Section 77 advances another step in the direction of liberalizing the law on the subject of bankruptcies. Railway corporations had been definitely excluded from the operation of the law in 1910 (c. 412, § 4, 36 Stat. 838, 839), probably because such corporations could not be liquidated in the ordinary way or by a distribution of assets. * * *
>
> "Equity receiverships, resorted to for that purpose, have never been satisfactory, for many reasons. Partly, no doubt, in recognition of that situation, Congress, by § 77, added railroad corporations to the category of those who might have relief by legislation passed in virtue of the bankruptcy clause of the Constitution; * * * Obviously, § 77 does no more than follow the line of historical and progressive development projected by previous acts" (pp. 671, 672).
>
> "* * * By § 2 of the Bankruptcy Act (U. S. C. Title 11, § 11), courts of bankruptcy are invested 'with such jurisdiction at law and in equity as will enable them to exercise original jurisdiction in bankruptcy proceedings.' *They are essentially courts of equity*, and their proceedings inherently proceedings in equity. * * * Their adjudications and orders constitute in all essential particulars decrees in equity" (p. 675). (Italics ours.)

Chapter XV is another step in the direction of liberalizing the law on the subject of railroad bankruptcy and the language of Mr. Justice Sutherland is equally applicable to the provisions thereof, in that it "does no more than follow the line of historical and progressive development projected by previous acts".

Courts of equity have always applied the doctrine in the absence of a statute that one who creates, protects or preserves a common fund may be compensated at the discretion of the court for his services, reasonable expenses and counsel fees. Courts of equity have time and again stated that such beneficial services should not go unrewarded and those receiving the benefits should be held accountable therefor.

*Trustees* v. *Greenough,* 105 U. S. 527.
*Central R & B Co.* v. *Petters,* 113 U. S. 116.
*Hobbs* v. *McLean,* 117 U. S. 567.
*U. S.* v. *Equitable Trust Co.,* 283 U. S. 738.

Judge Cardozo, in *Schoenherr* v. *Van Meter,* 215 N. Y. 548, 552, under circumstances not dissimilar to the instant case, said:

> "* * * The plaintiff rendered services of value, which the corporation has appropriated without requital. The plastic remedy of an equitable lien is adequate in such a case to prevent a failure of justice (*Perry* v. *Board of Missions,* 102 N. Y. 99, 105; *Meighan* v. *Am. Grass Twine Co.,* 154 Fed. Rep. 346)."

In *Siebert* v. *Minneapolis & St. L. Railway Co.,* 58 Minn. 58, the Court said at page 64:

> "And if, for any reason, the bondholders are permitted to appear in the action for the purpose of protecting the trust property, and do, in whole or in part, what the trustee might have thus done, it seems to us that there can be no doubt of the power of the court, upon a proper showing, to make the same reimbursement to them which it might have made to the trustee had he performed the same services and incurred similar expenses."

*In the instant case the Committee did what the Indenture Trustee failed to do: protect the interests of the Income Bondholders.*

Nor is it necessary where beneficial services have been rendered that the fund be in court in order to award allowances.

In *Forrester* v. *B. & M. Consol. Copper and Mining Co.*, 29 Mont. 397, 407, 74 Pac. 1088, 1099, the corporation contended that the plaintiffs who had rendered beneficial services to it were not entitled to any allowance for their services because there was no fund in the hands of the Court. This theory was completely rejected by the Court in the following language:

> "We can see no reason why the power of the court to allow an attorney fee should be made to depend upon the mere possession of the trust fund. * * * The allowance of such fee and the determination of the amount by the Chancellor have become the settled practice in courts of equity."

See also:

*Colley* v. *Wolcott*, 187 Fed. 595.
*Kilby* v. *Movius*, 55 N. D. 830.
*Mecartney* v. *Guardian Trust Co.*, 280 Fed. 64.
*U. S.* v. *Equitable Trust Co.*, 283 U. S. 738.
*First National Bank* v. *LaSalle-Wacker Building Corp'n*, 280 Ill. App. 188.

The aforesaid cases support the proposition that a court of equity may compensate those individuals who have aided in the administration of an estate even where no fund may have been brought into court.

The fact that Chapter XV does not specifically provide for the payment of fees does not preclude the Special Court, sitting as a court of equity, from exercising its sound discretion to award allowances to anyone who has intervened in the proceedings, and who has rendered valuable services to the railroad and its security holders. The provisions contained in other chapters of the Bankruptcy Act with respect to allowances are not special man-

dates given to a District Court Judge, but are merely a reiteration and restatement of sound equitable principles enunciated in equity of awarding allowances to those rendering beneficial services to an estate.

In an article entitled *"Fees and Expenses Under 77B"*, 34 Mich. L. Rev. 331, by George F. Medill, the author said as follows:

> "* * * The provisions of the Section touching allowances of compensation for services and reimbursement for expenses are no more than a restatement of the principles and practice of courts of equity in administration suits. Allowances to those officially in charge of trust property are made because the property must bear the expense of its administration. Allowances to others from the common property are a recognition and enforcement of the right of contribution by which the expense and burdens borne by a few in the accomplishment of the purposes of the Section are equitably distributed among all who have benefited. Control over agreements, indentures and authorizations required by the Section only express the solicitude courts of equity have always shown when dealing with fiduciary relationships. The court has full power and authority, and is required, to apply to fees and expenses the principles and the practice of courts of equity". (at p. 365)

The omission of any provisions in Chapter XV for allowances indicates that Congress intended to leave it to the sound discretion of the Special Court vested with all the powers of a court of equity and bankruptcy to make allowances should a situation arise where intervenors have rendered necessary and beneficial services to the debtor railroad and its creditors. Any other construction does violence to common sense and justice.

In *Grier* v. *Kennan,* 64 F. (2d) 605, the Court said at page 607:

> "The paramount duty of the court in construing a statute is to ascertain and give effect to the legislative intent. * * *

"So, in *United States ex rel. Gottlieb* v. *Commissioner of Immigration* (C. C. A. 2), 285 F. 295, it is held that 'in construing statutes, it is the duty of the court to endeavor to ascertain the intention and policy of Congress in their enactment, and to make practical application of that intention to the facts of the case'. *A particular construction must not produce inequality and injustice if another and more reasonable interpretation is possible.* *Knowlton* v. *Moore,* 178 U. S. 41, 20 S. Ct. 747, 44 L. Ed. 969.

'All laws should receive a sensible construction. General terms should be so limited in their application as not to lead to injustice, oppression, or an absurd consequence, and it will always be presumed that the legislature intended exceptions to its language, which would avoid results of this character.' *United States* v. *Kirby,* 7 Wall. 482, 483, 19 L. Ed. 278.

"The legislative intent must be determined from the act as a whole with especial regard to the circumstances surrounding the Legislature at the time of its enactment; and '*remedial statutes will be liberally construed, to give effect to the humane* purpose of the Legislature'. *Camunas* v. *New York & P. R. S. S. Co.* (C. C. A. 1), 260 F. 40, Rev. St. U. S. Sec. 1042 (section 641, 18 U. S. C. A.), is a remedial statute. *United States* v. *Pratt* (D. C.), 23 F. (2d) 333, 334." (Italics ours.)

The Bankruptcy Act is remedial in its nature and as such must be reasonably and liberally construed as to promote justice and equity (*Botts* v. *Hammond,* 99 Fed. 916, 920; *Manly* v. *Hood,* 37 Fed. [2] 212, 215).

Chief Justice Hughes in *Reconstruction Finance Corporation* v. *J. G. Menihan Corporation et al.,* decided February 3, 1941, by the Supreme Court, 85 Law. Ed. 458, said:

"* * * The defendants have successfully resisted the charge, *and the question is whether they should be denied the usual incidents of their success.* * * * The additional allowance made by courts of equity in accordance with sound equity practice is likewise such an incident (*Sprague* v. *Ticonic Bank,* 307 U. S. 161). We perceive no reason for holding that petitioner may avail itself of the judicial process in accordance with the authority conferred upon it and escape the usual

incidents of that process in case its assertions of right prove to be unfounded * * *" (at p. 460). (Italics ours.)

By this decision the petitioners believe that the Supreme Court has declared the principle that litigants, who are brought into court in any proceeding, or who have been permitted to intervene therein to protect their interests, whose services have been successful and beneficial, should not be "denied the usual incidents of their success".

## II

**Section 725(6) does not preclude the Special Court from awarding the Committee and its counsel allowances herein.**

Section 725(6) provides as follows:

"(6) That, after hearing for the purpose, all amounts or considerations, *directly or indirectly paid or to be paid by or for the petitioner for expenses, fees, reimbursement or compensation of any character whatsoever incurred in connection with the proceeding and plan,* or preliminary thereto *or in aid thereof,* together with all the facts and circumstances relating to the incurring thereof, have been fully disclosed to the Court so far as such amounts or considerations can be ascertained at the time of such hearings, that all such amounts or consideration are fair and reasonable, and to the extent that any such amounts or considerations are not then ascertainable, the same are to be so disclosed to the Court when ascertained, and are to be subject to approval by the special court as fair and reasonable, and except with such approval no amounts or considerations covered by this clause (6) shall be paid." (Italics ours.)

The purpose of this section is clearly stated by Judge Chestnut in the *Baltimore & Ohio* case, *supra,* at page 158:

"The evident purpose of the requirement of section 1225(6) of Chap. 15 is, in the interest of the security

> holders of the corporation, that funds which might otherwise be applicable to payment on their securities, shall not be wasted or lavishly disbursed for purposes or in amounts *other than are reasonably and properly necessary for successful prosecution of the Plan.*" (Italics ours.)

It cannot be successfully argued that Congress intended by this section to prevent and deprive security holders, not otherwise represented, from having a committee and counsel intervene in their behalf to protect their interest and to have the expenses incurred therewith paid by the petitioner railroad if such representation was necessary and the results derived beneficial not only to the security holders but to the railroad itself. The only intent of said section was to provide that all expenses incurred by the petitioner railroad must be disclosed to the Court in order that it may determine whether such amounts are fair and reasonable. There is nothing in the section which directly or indirectly precludes or prohibits the Court from granting allowances to intervenors where they have rendered beneficial services.

Petitioners respectfully submit that if the Special Court had power to make an allowance to the railroad company and counsel for the Indenture Trustee under the aforesaid section*, it had equal power to grant allowances to the Committee and its counsel for their services, which were necessary to the effectuation of a fair and equitable plan.

The Special Court, in concluding that it had no jurisdiction to award allowances to Committee and its counsel erroneously followed the opinion rendered *In re Baltimore & Ohio R. R. Co., supra,* and the order entered *In re Lehigh Valley Railroad Company,* 34 F. Supp. 753.

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* The Order Supplemental to Decree authorized the payment of $2,000 to counsel for the Indenture Trustee. The Court said in its opinion:

> "*B.* Under the broad language of Title II, United States Code, Section 1225 (6), above quoted, we think we have the power to deal with the expenses and allowances to the petitioner and counsel for the Indenture Trustee."

Petitioners respectfully submit that the Special Courts sitting in the *Baltimore & Ohio* and the *Lehigh Valley Railroad* cases, *supra,* mistakenly based their denial of allowances on jurisdictional grounds instead of on the merits.

In both cases it appears that the individual intervenors rendered no beneficial services as the plans of adjustment were approved by the Special Courts without modification. The Special Courts, in said cases, may have reached the proper result; but their reasoning, predicated on jurisdictional grounds, was improper and contrary to the intent and provisions of Chapter XV. The Special Courts therein adopted the line of least resistance and thus unwittingly injured the cause of all meritorious applications by intervenors which might follow in subsequent proceedings under Chapter XV.

Furthermore, in the instant case, the adjustment differed from the adjustments in the aforesaid cases in that: (a) the petitioning railroad (Peoria Company) was not independently represented in the proceedings as it was controlled and dominated by the New York Central, its majority stockholder, lessee and creditor, whose interests were adverse to the Peoria Company and its security holders; (b) the Plan of Adjustment, in addition to the modification and extension of a portion of its bonded indebtedness, provided for the extension and modification of the operating agreement between the New York Central and Peoria Company which directly affected the interests of the Income Bondholders; and (c) the Income Bondholders as a class were not afforded an opportunity to express their approval or disapproval of the adjustment as the same affected their securities except through the intervention of the Committee and its counsel.

It is significant to note that the Special Court in the *Lehigh Valley* case with the consent of the Lehigh Valley Railroad Company awarded to counsel for the Bondholders' Committee the sum of $35,000 as and for their compensation.

**Can it be successfully contended that when a debtor railroad makes an agreement with a friendly committee for compensation, that agreement shall be approved by the Court, but when a committee, independent of the railroad, renders necessary and beneficial services without having first secured the approval and the consent of the railroad, then the Court is precluded from awarding any compensation?**

It is unreasonable to assume that Congress had such intention when it drafted Chapter XV. Such a construction of 725(6) is equivalent to an usurpation of the Court's inherent equity power to make allowances for beneficial and necessary services rendered in the administration of an estate, and would thereby deprive the Court from having the benefit and assistance of counsel representing creditors independent of the debtor railroad to direct the attention of the Court to such facts as are necessary to enable it to determine whether the plan as promulgated by the railroad "is fair and equitable as an adjustment, affords due recognition to the rights of each class of creditors. * * *" as is required under Section 725(3) (11 U. S. C. A. 1225[3]).

Under Chapter XV, as under every chapter of the Bankruptcy Act, the Court is a court of equity. To deny the Committee and its counsel, who, in good faith, rendered the valuable services aforementioned, compensation merely because they were not actually retained by the Peoria Company, thwarts the intent of Congress, results in a gross injustice and penalizes rather than rewards the Committee and its counsel for their services herein.

## Prayer for Writ

WHEREFORE, petitioners respectfully pray that a writ of certiorari be issued under the seal of this Court, directed to the District Court of the United States for the Southern District of New York, to the end that this cause may be reviewed and determined by this Court and the order of

the District Court of the United States denying allowances to the Committee and its counsel may be reversed, and that petitioners may have such other and further relief as this Court may deem proper in the premises.

Dated: New York City, June 4, 1941.

WM. CARNEGIE EWEN, LEWIS L. CLARKE, M. D. ADAMS and GEORGE E. WILE, as members of a duly constituted Income Bondholders' Protective Committee, and CHARLES S. ARONSTAM, Counsel to the Committee,

By CHARLES S. ARONSTAM,
Counsel.

## APPENDIX "A"

The portion of the Opinion of the Special Court, dated April 3, 1941, pertaining to allowances is hereinafter set forth:

UNITED STATES DISTRICT COURT

SOUTHERN DISTRICT OF NEW YORK

| | |
|---|---|
| IN THE MATTER OF THE PEORIA & EASTERN RAILWAY COMPANY, Petitioner. | IN PROCEEDINGS FOR A RAILROAD ADJUSTMENT<br>No. 76,016 |

* * * * * * *

III. *A.* By way of preface to the question of allowances, it seems to us appropriate to observe that a proceeding for a Railroad Adjustment under Chapter 15 of the Bankruptcy Act,—Title 11 United States Code, Sections 1200 to 1255—which is now terminated by reason of its own limitations,—Cf. Section 1255—was a proceeding commenced by a petition which was to be addressed in an appropriate *venue* to a Three-Judge Court given equity jurisdiction for a limited purpose, namely, to determine whether the adjustment sought by the petitioner was equitable and should be allowed. The Court did not take possession of any property or funds. The appearance of any other party than the petitioner in such a proceeding depends solely on the appropriate exercise of the judicial discretion of the Court, and any such party could come in only by way of intervention based on the intervenor's petition. For Chapter 15 of the Bankruptcy Act—Title 11 United States Code, Sections 1200-1255—does not provide for any adversary proceedings.

Consequently, it seems to us that we must look only to the provisions of Title 11 United States Code, Section 1225(6) to determine our jurisdictional competence to grant allowances.

Section 1225(6), in so far as it is relevant here, provides as follows (italics ours):

"That, after hearings for the purpose, all amounts or considerations, *directly or indirectly paid or to be paid by or for the petitioner* for expenses, fees, reimbursement or compensation of any character whatsoever incurred in connection with the proceeding and plan, or preliminary thereto or in aid thereof, together with all the facts and circumstances relating to the incurring thereof, have been fully disclosed to the Court so far as such amounts or considerations can be ascertained at the time of such hearings, that all such amounts or considerations are fair and reasonable, and to the extent that any such amounts or considerations are not then ascertainable, the same are to be so disclosed to the Court when ascertained, and are to be subject to approval by the special court as fair and reasonable, and except with such approval no amounts or considerations covered by this clause (6) shall be paid."

*B.* Under the broad language of Title 11 United States Code, Section 1225(6), above quoted, we think we have power to deal with the expenses and allowances to the petitioner and the counsel for the Indenture Trustee.

We find that the expenses above detailed are fair and reasonable as required by that Section. We also allow fees to the counsel for the Indenture Trustee, which we fix at the sum of Two thousand dollars ($2,000).

*C.* The petitions for allowances made by the counsel for the intervenors are, however, in all respects denied for want of jurisdiction.

It seems to us clear that Chapter 15 of the National Bankruptcy Act covering Railroad *Adjustments,* in so far

as allowances to others than the petitioner Railway are concerned, is not in *pari materia* with Title 11 United States Code, Section 205, which deals with the *Reorganization* of Railroads. That Section provides, in so far as it is here relevant, as follows (italics ours):

"(c) * * * (12) Within such maximum limits as are fixed by the Commission*, the judge may make an allowance * * * for the actual and reasonable expenses (including reasonable attorney's fees) incurred in connection with the proceedings and plan by *parties in interest and by reorganization managers and committees or other representatives of creditors and stockholders,* and within such limits may make an allowance out of the debtor's estate for the actual and reasonable expenses incurred in connection with the proceedings and plan and reasonable compensation for services in connection therewith by trustees under indentures, depositaries and such assistants as the Commission with the approval of the Judge may especially employ. * * *"

It will be seen, therefore, that a special mandate is given to the Judge, in a reorganization proceeding under the Section quoted, to make allowances for reasonable expenses, including reasonable attorney's fees incurred in connection with the proceeding and plan by the parties interested, and also including committees of creditors.

It seems to us that the omission of such a provision from Chapter 15 of the National Bankruptcy Act, which gave a Three-Judge Court jurisdiction in *Proceeding for Railway Adjustment,* makes it quite clear that we have not any jurisdiction properly to grant any allowances herein to the intervenors or their counsel.

This result was reached by a Three-Judge Court in the District of Maryland *In re Baltimore & Ohio R. R. Co.,* 34 F. Supp. 154, 160; and we are told also in the Eastern District of Pennsylvania in the case of *In re Lehigh Valley Railroad Company,* 34 F. Supp. 753. In that case the

* The Interstate Commerce Commission.

*Baltimore & Ohio* case is not mentioned in the opinion, but it is cited with approval in an order which was entered on October 21, 1940, denying petitions for compensation to counsel representing the security holders.

In the *Baltimore & Ohio* case, 34 F. Supp. 154, Judge Chestnut, speaking for a Three-Judge Court constituted under Chapter 15 and consisting of Parker and Dobie, Circuit Judges, and himself, gives at page 160 a very good reason why a Three-Judge Court, under Chapter 15 of the National Bankruptcy Act, has not jurisdiction to grant allowances to intervenors: namely, that it is not a court of equity with general jurisdiction over property or a fund in Court with the incidental power to make allowances to parties who have helped secure or conserve that property or fund, but is a court of equity which is limited to a personal jurisdiction only by the statute, which provides for its creation, and fixes its jurisdictional competence.

We cannot, however, close our opinion without telling counsel for the two intervenors that we welcomed their participation in this cause, that by the modifications in the plan which they suggested, in our opinion, they made a valuable contribution to the creation of a fair and reasonable adjustment herein under which the parties will have to operate for many years to come, and that if we had felt that we were authorized by Chapter 15 of the National Bankruptcy Act to grant them or their counsel a reasonable allowance, we should have done so.

April 3, 1941.

(6)

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IN THE

# Supreme Court of the United States

OCTOBER TERM, 1941.

No. 144.

WILLIAM CARNEGIE EWEN, *et al.*,
*Petitioners,*

*against*

THE PEORIA AND EASTERN RAILWAY COMPANY,
*Respondent.*

## BRIEF OF RESPONDENT IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI.

JACOB ARONSON,
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July 1, 1941.

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## BRIEF OF RESPONDENT IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI.

### Statement.

Petitioners herein are members of a committee, styled Income Bondholders Protective Committee, representing certain of the holders of the Income Bonds of The Peoria and Eastern Railway Company and their counsel.

Petitioners' application for allowances, the denial of which is now sought to be reviewed, was made in a proceeding under Chapter XV, originally numbered as Sections 700 to 755, of the Bankruptcy Act (Title 11, U. S. Code, Sections 1200-1255).* By Section 1200, the Bank-

* NOTE: The references to sections herein are in accordance with the numbering contained in Titie 11, U. S. Code.

ruptcy Court was authorized to exercise original jurisdiction as provided in said Chapter XV for "postponements or modifications of debt, interest, rent, and maturities or for modifications of the securities or capital structures of railroads." As provided in Section 1255, the jurisdiction conferred by Chapter XV terminated on July 31, 1940, except as to proceedings pending at that time.

The Peoria and Eastern brought proceedings pursuant to such Chapter XV in January of 1940 for the approval of a Plan of Adjustment in respect of its Consolidated Bonds, which Plan had been assented to as provided in such Chapter and was, following approval thereof by the Interstate Commerce Commission pursuant to Section 1210, approved on June 29, 1940, by the Special Court convened pursuant to Section 1213. The petitioners had opposed approval of the Plan. The opinion of the Court approving the Plan is reported in 34 Fed. Supp. 332, and applications for certiorari by petitioners and a committee representing certain minority Consolidated Bondholders were denied (311 U. S. 700).

Thereafter, petitioners herein and the minority committee of the Consolidated Bondholders applied for allowances. Such applications were denied by the Special Court on April 3, 1941, in an opinion by Judge Woolsey (Record, pp. 10-17; reported 37 Fed. Supp. 917). Application for reargument by petitioners herein (in which the committee of Consolidated Bondholders did not join) was denied in a memorandum by the Special Court under date of April 18, 1941 (Rec., p. 36). The committee of Consolidated Bondholders has not joined in the pending petition for certiorari.

The Special Court in its opinion (34 Fed. Supp. 332, 338) had required that the Plan be modified so as to provide that the Income Bondholders should have one director upon the

Board of the Peoria and Eastern. The claim of petitioners for an allowance is largely based upon this modification which the Court held did not substantially affect the rights of any class of creditors and did not require resubmission to the Interstate Commerce Commission or security holders.

Petitioners' contention (petition, p. 3), that recital in the supplemental decree with reference to indebtedness of the Peoria and Eastern to the New York Central was a modification of the Plan insisted on by petitioners, is misleading. That the accounts in question were wholly unrelated to the Plan and that the Special Court made no disposition of such accounts appears from the opinion of Judge Learned Hand (34 Fed. Supp. 332, 336), as follows:

> "The Accounts between the New York Central and the Peoria & Eastern.
>
> "Not only has a large operating deficit accumulated against the Peoria & Eastern, but a large 'retirement' account and a large 'depreciation' account have accumulated in its favor against the New York Central. The plan does not liquidate either of these, and the order of confirmation will leave open all questions touching their amount and validity. If the New York Central seeks in any year to withdraw any part of the earnings by way of recoupment, it must prove its right. All we now hold is that the covenant to maintain the road and to make additions to its equipment, did not contemplate gratuitous advances, and that the third article allowed recoupment for so much as was properly expended. Whether the cross items can be offset, the plan also leaves open."

## Petitioners' Application for Allowances Was Properly Denied.

The matter of allowances under Chapter XV of the Bankruptcy Act has been considered by Special Courts convened in three cases, the *Baltimore and Ohio Case,* the *Lehigh Valley Case* and the instant case. In each, the Court found that under the terms of said Chapter it has no jurisdiction to grant allowances.

*In re Baltimore & O. R. Co.,* 34 Fed. Supp. 154, 160, District Judge Chesnut, writing for the three-judge Court consisting of Circuit Judges Parker and Dobie and himself, said:

> "(4) Counsel for certain security holders allowed to intervene in this case, who personally participated in the hearings, have asked the court for allowances for fees for their services, to be paid by the B and O. These counsel represented the holders of securities of several issues in the amount of about $50,000. The general position of some of them was not nominally opposed to the Plan as a whole, but to obtain modifications of the Plan in certain respects for the benefit and advantage of their respective clients. Nevertheless the general effect of the success of the opposition by all of them would practically have been to defeat the Plan. *The court was very glad to have these counsel participate in the case and to hear and consider their arguments. They were helpful in an understanding of the issues involved and clarifying the questions debated, and to some extent in criticizing and suggesting changes in the supplemental indenture and modifying agreements.* We are, however, of the opinion that we have no authority under the Act to make the allowances. The nature of the case is not one where a court of equity has general jurisdiction over a fund in court, with incidental

> power to make allowances out of the fund to counsel or parties who have performed services to bring the fund into court or to preserve it. The provision of the Act in section 1225 (6) with regard to approval of expenditures of the petitioners including legal expenses is the only reference to the subject in the whole Act. The legislative history of the passage of the Act referred to by counsel affords no indication that it was the intention of Congress to authorize the court exercising the special jurisdiction in this case to make such allowances to counsel for security holders appearing in opposition to the Plan, or seeking modifications of it. In this respect the Act is quite different from former Section 77B and the present Chapter 10 of the Bankruptcy Act. We are unable, therefore, to make the allowances requested." (Italics ours.)

Certiorari was denied, 311 U. S. 717.

In the *Lehigh Valley Railroad Company Case,* before a Special Court consisting of Circuit Judge Maris and District Judges Welsh and Kalodner, a similar application by intervenors in that case was denied in an order entered on October 21, 1940, reading as follows:

> "The petitions of Meyer Abrams, Samuel Paul Puner, Isadore H. Schweidel, Cecil M. Page, Stewart M. Seymour, and Edith A. Merrit for the allowance or approval of fees or compensation for services and reimbursement of expenses not authorized by the petitioners are dismissed for want of jurisdiction in this court to entertain them (See in re *Baltimore & O. R. Co.,* 34 F. Supp. 154)."

Certiorari was denied February 3, 1941 (85 L. Ed. 492).

In the instant case, the opinion (Rec., pp. 16-17) of Judge Woolsey (concurred in by the other two members of the special bench, to wit, Circuit Judge Learned Hand and

District Judge Hulbert) points out the dissimilarity, as to allowances, between Chapter XV of the Bankruptcy Act, dealing with Adjustments, and Section 205 of the Bankruptcy Act, covering Railroad Reorganizations.

The reason for the distinction, with respect to allowances, between Chapter XV and the other chapters of the Bankruptcy Act dealing with railroad and non-railroad reorganizations, referred to as Sections 77 (now Section 205, U. S. Code) and 77B (now Sections 501 *et seq.*, U. S. Code), is clear. In proceedings under Sections 77 and 77B the Court takes charge of the property and administers it. It assumes complete possession, which is exercised through its appointees, so that it has a fund in its custody that becomes subject to its disposition, as is the familiar situation in equity. Here, however, the Court does not have custody and possession of the estate, and its only jurisdiction with respect to the property of the Railway Company is the jurisdiction provided in Section 1215, empowering it during the pendency of the proceedings to protect the Railway Company and its property

> "against any action which might be inconsistent with said plan of adjustment or might interfere with the effective execution of said plan if approved by the court, or otherwise inconsistent with or contrary to the purposes and provisions of this chapter: *Provided, however,* That nothing herein contained shall be construed to authorize the court to appoint any trustee or receiver for said properties or any part thereof, or otherwise take possession of such properties or control the operation or administration thereof."

Notwithstanding the complete absence of any provision of the statute authorizing the making of allowances, petitioners argue that Section 1213, by implication, invests the

Court with necessary power. Apparently petitioners construe the provision in question as if the latter part thereof, italicized in the following quotation, did not exist, to wit:

> "Such three-judge court shall be vested with and shall exercise all the powers of a district court sitting in equity and all the powers as a court of bankruptcy *necessary to carry out the intent and provisions of this chapter, including the classification of claims at such time and in such manner as the court may direct.*"

The matter of fees and expenses is specifically covered in subdivision (6) of Section 1225, as follows:

> "(6) That, after hearings for the purpose, all amounts or considerations, directly or indirectly paid or to be paid by or for the petitioner [the Railway Company] for expenses, fees, reimbursement or compensation of any character whatsoever incurred in connection with the proceeding and plan, or preliminary thereto or in aid thereof, together with all the facts and circumstances relating to the incurring thereof, have been fully disclosed to the Court so far as such amounts or considerations can be ascertained at the time of such hearings, that all such amounts or consideration are fair and reasonable, and to the extent that any such amounts or considerations are not then ascertainable, the same are to be so disclosed to the Court when ascertained, and are to be subject to approval by the special court as fair and reasonable, and except with such approval no amounts or considerations covered by this clause (6) shall be paid."

Chapter XV is the part of the Bankruptcy Act dealing exclusively and comprehensively with *adjustments,* as distinguished from *reorganizations,* which are governed by other provisions of the Act. Since Chapter XV carries its own provision, above-quoted, governing allowances, it

seems manifest that such provision was intended to be exclusive as to adjustments under that Chapter. The obvious contemplation of Chapter XV was that intervenors should bear their own law expenses, or if employed by others should, as is the usual situation, look to them for their fees.

Furthermore, petitioners in the instant case were not even *affected* by the Plan of Adjustment approved by the Court. Sections 1210 and 1225 provide for assents by specified percentages of all claims *affected* by the Plan as conditions to (1) submission to the Interstate Commerce Commission, (2) filing of the Plan in Court, and (3) approval by the Court.

The Court in its findings in respect of the Plan (Rec., pp. 25-26) found that the only claims *affected* by the Plan were the First Consolidated Bonds; that consents of the Income Bondholders to the Plan had not been solicited or secured; that the Plan had been accepted by more than the required percentage of First Consolidated Bonds; and that the Plan had been accepted in accordance with Chapter XV of the Bankruptcy Act. The petitioners were authorized to intervene as persons in interest under Section 1220, not as parties *affected* by the Plan. The Court in the instant case, as in the *Baltimore and Ohio Case*, welcomed the participation of the intervenors and considered it helpful.

Indeed, it would appear that the petitioners, who have been held not to be *affected* by the Plan, are without legal authority to apply for certiorari. Section 1245, which is the only jurisdictional authority invoked by petitioners (their petition, p. 4), reads as follows:

> "Any final order or decree of the special court may be reviewed by the Supreme Court of the United States upon application for certiorari made by any person *affected by the plan* who deems himself

aggrieved within sixty days after the entry of such order or decree, pursuant to the provisions of the Federal Judicial Code." (Italics ours.)

Furthermore, since Chapter XV lapsed by its own limitation (Section 1255) as of July 31, 1940, with the exception of any cases then pending (and so far as we know the Peoria and Eastern was the last), the pending question is moot except as to the immediate parties. As shown above, Special Courts in two separate circuits, in addition to the Special Court in the instant case, have ruled adversely to the construction of the Adjustment statute now urged by petitioners. The Supreme Court denied certiorari in both cases, the application in the *Lehigh Valley Case* relating solely to the question of allowances.

Accordingly, it is submitted that the order below was right, that the issue is no longer an open one and that in no aspect are any questions involved which warrant review.

Respectfully submitted,

JACOB ARONSON,
CROSBY J. BEAKES,
JOHN PURYEAR,
Counsel for Respondent.

July 1, 1941.

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IN THE

# Supreme Court of the United States

OCTOBER TERM 1941

No. 144

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WM. CARNEGIE EWEN, LEWIS L. CLARKE, M. D. ADAMS and GEORGE E. WILE, as members of a duly constituted Income Bondholders' Protective Committee, and CHARLES S. ARONSTAM, Counsel to the Committee,

*Petitioners,*

against

THE PEORIA AND EASTERN RAILWAY COMPANY,

*Respondent.*

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## REPLY MEMORANDUM OF PETITIONERS IN SUPPORT OF PETITION FOR WRIT OF CERTIORARI

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CHARLES S. ARONSTAM,
Counsel for Petitioners.

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## REPLY MEMORANDUM OF PETITIONERS IN SUPPORT OF PETITION FOR WRIT OF CERTIORARI

Although counsel for the New York Central Railroad Company, who are also counsel for the respondent, attempt, at the outset of their brief, to minimize the services rendered herein by petitioners, the opinion of the Special Court speaks for itself:

> "that by the modifications in the plan which they suggested, in our opinion, they made a valuable contribution to the creation of a fair and reasonable adjustment herein under which the parties will have to operate for

> many years to come, and that *if we felt that we were authorized by Chapter 15 of the National Bankruptcy Act to grant them or their counsel a reasonable allowance, we should have done so*" (Record, p. 17). (Italics ours.)

Petitioners are entitled to be compensated for their services in accordance with the established principles of equity as enunciated in *Trustees* v. *Greenough*, 105 U. S. 527, and *Sprague* v. *Ticonic Bank*, 307 U. S. 161.

In *Trustees* v. *Greenough, supra,* the Court said:

> "It is a general principle that a trust estate must bear the expenses of its administration" (at p. 532).

In *Sprague* v. *Ticonic Bank,** *supra,* plaintiff instituted suit on her own behalf to affix a lien on earmarked funds in an insolvent bank for the repayment in full of a sum theretofore deposited by her in trust. After establishing her lien, plaintiff petitioned the District Court for reasonable counsel fees and litigation costs to be paid out of fourteen trusts in situations similar to her own, contending that by reason of her efforts, she established, as a matter of law, their right to recovery in the same manner as her own right. The District Court denied the petition on the ground that it did not have the power to grant such an allowance. Mr. Justice Frankfurter, in upholding the right of plaintiff to the allowances prayed for, said:

> "Allowance of such costs in appropriate situations is part of the historic equity jurisdiction of the federal courts" (at p. 164).
>
> "That the party in a situation like the present neither purported to sue for a class nor formally established by litigation a fund available to the class, does not seem to be a differentiating factor so far as it affects the

* The opinion in this case supports the contention of petitioners that it is not necessary for a fund to be in court for equity to grant an allowance where necessary and beneficial services have been rendered to a trust estate.

source of the recognized power of equity to grant reimbursements of the kind for which the petitioner in this case appealed to the chancellor's discretion. *Plainly the foundation for the historic practice of granting reimbursement for the costs of litigation other than the conventional taxable costs is part of the original authority of the chancellor to do equity in a particular situation*" (at p. 166). (Italics ours.)

"As in much else that pertains to equitable jurisdiction, individualization in the exercise of a discretionary power will alone retain equity as a living system and save it from sterility. In the actual exercise of the power to award costs 'as between solicitor and client' all sorts of practical distinctions have been taken in distributing the costs of the burden of the litigation" (at p. 167).

The Special Court held that it was precluded from awarding any allowances except as approved by the respondent by reason of the provisions of Section 725(6) of Chapter XV (11 U. S. C. A. 1225(6)). Section 725(6) was inserted in Chapter XV for the sole purpose of having the Special Court control and police the expenses incurred by the debtor railroad in connection with the consummation of a plan of adjustment. As stated by Judge Chestnut in *In re Baltimore & Ohio R.R. Co.*, 34 Fed. Supp. 154, this provision was for the protection of security holders so that "funds which might otherwise be applicable to payment on their securities, shall not be wasted or lavishly disbursed for purposes or in amounts other than are reasonably and properly necessary for successful prosecution of the Plan."

If the sole purpose of Section 725(6) was for the protection of security holders, Congress could not have intended thereby to preclude the Special Court from awarding compensation to intervenors in cases where their services were necessary and beneficial to the security holders.

The Report of the Senate Committee on Interstate Commerce (Report No. 489, 76th Congress, First Session) states,

among other things, the purpose of this legislation as follows:

> "(3) to safeguard the public interest and the interest of investors in any application of the bill if enacted."

**In the case at bar the only way the Income Bondholders as a class could be protected was by the independent intervention of the petitioners.**

In the light of the foregoing it is respectfully submitted that Section 725(6) does not preclude the Special Court from exercising its equity power, as set forth in Section 713 (11 U. S. C. A. 1213), to award petitioners compensation for their valuable services herein. It would require unequivocal language to compel the conclusion that Congress intended, in proceedings under Chapter XV, to preclude the Special Court sitting as a court of equity from exercising its historic right to award allowances to those who aid in the administration of a trust estate.

Respondent initiated these proceedings solely for its own benefit. The Income Bondholders were forced to intervene to protect their interests and the respondent, in equity and good conscience, should bear the expenses incident thereto.

The principle enunciated in *In re Watco Corporation,* 95 F. (2d) 249, is applicable to the facts herein. In that case the Court said:

> "* * * it is as important that fees for meritorious services actually rendered and necessary to effectuate a reorganization should be allowed as it is that the court should prevent the undue enrichment of attorneys for services of no value to the debtor" (at p. 251).

Respondent asserts in its brief that, under Section 745 of Chapter XV (11 U. S. C. A. 1245) the petitioners are without legal authority to petition this Court for a writ of certiorari, on the ground that the Income Bondholders were not affected by the Plan. There can be no doubt that the Income Bondholders were adversely affected by the terms and provisions of the Plan of Adjustment as promulgated

by the respondent, as evidenced by the modifications to the Plan made by the Special Court at the instance and request of the petitioners who represented the Income Bondholders as a class.

The realistic and equitable approach to the matter of compensation as presented herein is embodied in the opinions of Judge Cardozo in *Schoenherr* v. *Van Meter,* 215 N. Y. 548, 552; Mr. Justice Frankfurter in *Sprague* v. *Ticonic National Bank,* 307 U. S. 161, 164, 166, 167, and Mr. Justice Hughes in *Reconstruction Finance Corporation* v. *J. G. Menihan Corporation et al.,* 85 Law. Ed. 458, 460. In each of these cases the Court brushed aside technicalities to the end that justice might be done to those who rendered beneficial services to a trust estate.

It is apparent that the order of the Special Court denying compensation to the petitioners on jurisdictional grounds, despite the fact that the Court recognized that the services rendered were valuable and necessary, creates an unjust and harsh result.

The Committee and its counsel have labored unremittingly in excess of one year in their efforts to safeguard the interests of the Income Bondholders and respondent itself: and in that they have been successful. The order of the Special Court denying compensation to petitioners has so far departed from sound equitable principles as enunciated by this Court as to call for the exercise of this Court's power of supervision to the end that justice may be served.

Respectfully submitted,

CHARLES S. ARONSTAM,
Counsel for Petitioners.

July 17, 1941.